



Report on the Impact of Reducing the Lowest Marginal Personal Income Tax Rate on Non-Refundable Tax Credits

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Context

Pursuant to section 2.1 of the *Making Life More Affordable for Canadians Act*, this report has been prepared to examine the implications of reducing the lowest personal income tax rate under paragraph 117(2)(a) of the *Income Tax Act* on all tax credits calculated using the “appropriate percentage” as defined in the *Income Tax Act*.

Background

Bill C-4 reduced the lowest marginal personal income tax rate from 15 per cent to 14.5 per cent for the 2025 taxation year and to 14 per cent for the 2026 and subsequent taxation years. The intermediate rate approximates a one-percentage-point cut in the lowest tax rate coming into effect halfway through 2025. This tax cut is anticipated to save individuals up to \$420 and a two-income family up to \$840 in 2026 and generate tax savings for nearly 22 million Canadians. Bill C-4 received Royal Assent on March 12, 2026.

1. The Federal Personal Income Tax Rate Structure

Canada’s personal income tax system has a progressive rate structure, where tax rates increase with income. This reflects a key principle of vertical equity whereby those with a greater ability to pay are subject to higher taxes.

There are five income tax brackets with tax rates ranging from 14 per cent to 33 per cent, and bracket thresholds are indexed to inflation to keep up with the cost of living.

The lowest marginal tax rate of 14 per cent applies to the first \$58,523 (2026) of an individual’s taxable income. Each additional dollar earned above this threshold is taxed at higher rates, which gradually increase according to the structure shown in Table 1.

The Basic Personal Amount (BPA) is a non-refundable tax credit that functions as part of the rate structure by allowing individuals to earn up to \$16,452 (in 2026) before owing federal income tax.¹

Table 1
Federal personal income tax rate structure, 2026

Bracket	Taxable Income Threshold	Marginal Tax Rate
1	Up to \$58,523	14%
2	\$58,523 to \$117,045	20.5%
3	\$117,045 to \$181,440	26%
4	\$181,440 to \$258,482	29%
5	\$258,482 and over	33%

2. Non-Refundable Tax Credits

Most tax credits are non-refundable and reduce the amount of tax an individual owes, up to the point that the individual no longer owes tax. If an individual does not owe tax to begin with, they do not benefit from claiming non-refundable tax credits. In contrast, a credit is refundable when any excess of the credit over the amount of tax payable is refunded to the taxpayer. Thus, individuals can benefit from refundable tax credits even if they do not owe tax. Many refundable credits are designed as income-tested measures that provide income support (e.g., the Canada Workers Benefit).

Each credit has its own eligibility criteria. Most credits require an eligible expenditure to be made, such as the Tuition Tax Credit and the Charitable Donation Tax Credit, while some personal credits, such as the Basic Personal Amount, are available to all individuals without requiring any expenditure. The amount an individual can claim also varies by tax credit (see Table 2).

¹ The BPA is composed of a minimum amount (\$14,829 in 2026) that is available to all taxpayers, and a supplement (\$1,623 in 2026) that begins to phase out once an individual’s income reaches the fourth tax bracket (\$181,440 in 2026) and is fully phased out by the fifth-bracket income threshold (\$258,482 in 2026).

Table 2

Maximum credit amounts and claimants by tax credit

Credit Name	Maximum Credit Amount (2026)	Number of Claimants (2023)
Basic Personal Amount	\$16,452	31.2 million
Age amount	\$9,208	7.1 million
Eligible dependant amount	\$16,452	1.0 million
Spouse or common-law partner	\$16,452	2.3 million
Caregiver amounts	\$2,740 ¹	604,000
Base CPP or QPP contributions	\$4,230	20.4 million
EI or QPIP premiums	\$1,123	22.5 million
Volunteer firefighters' amount	\$6,000	464,000
Search and rescue volunteers' amount	\$6,000	6,200
Canada employment credit	\$1,501	20.1 million
Home buyers' amount	\$10,000	199,000
Home accessibility expenses	\$20,000	39,000
Adoption expenses	\$19,972 ²	1,570
Pension income amount	\$2,000	6.0 million
Disability amounts	\$10,341 ³	1.9 million
Student loan interest	n.a.	331,000
Tuition amounts	n.a. ⁴	3.0 million
Medical expenses	3% of net income	5.8 million
Charitable donations ⁵	\$200	5.0 million

Notes. The maximum credit amount reflects the amounts for the 2026 taxation year. Some tax credits do not have a maximum amount (as indicated by "n.a."). The number of claimants is based on the latest available taxpayer information (2023).

¹ Caregivers may be able to claim an additional \$8,773 in 2026 for an infirm dependant such as a child under 18 years of age, a dependant spouse or common-law partner, or an eligible dependant.

² This amount is the maximum amount per adoption.

³ This is the maximum amount that can be claimed for an adult. Individuals claiming the disability tax credit for a child with disabilities may be eligible for a maximum supplement of \$6,032 in 2026.

⁴ A student must first use their tuition amount to reduce their own tax payable. They can then transfer up to \$5,000 of the unused current-year tuition amount to a spouse, parent, or grandparent (including a spouse's parent or grandparent).

⁵ Only the first \$200 of an individual's charitable donation claim is subject to the lowest income tax rate. The total expenditure of the charitable donation tax credit accounts for all amounts claimed, including those exceeding \$200.

Non-refundable tax credits serve various policy objectives. These objectives can include recognizing expenses incurred to earn income (e.g., Canada Employment Credit), encouraging certain social or economic activities (e.g., Volunteer Firefighters Amount), and recognizing situations where individuals have a reduced ability to pay due to unavoidable or non-discretionary expenses (e.g., Medical Expense Tax Credit, Disability Tax Credit and Canada Caregiver Credit).

While they have different objectives, generally non-refundable tax credits are intended to offset the tax on income that was used to pay for the eligible expenses recognized by the credits (at the lowest personal income tax rate).

Most non-refundable tax credits have a maximum eligible amount that is indexed to inflation, just like tax brackets, to keep up with the cost of living. The value of a tax credit is determined by applying a credit rate to the applicable credit amount. The credit rate applied to most non-refundable tax credits (those listed in Table 2 above) is legislatively based on the lowest personal income tax rate (14 per cent in 2026). For example, if an individual is eligible for a credit with a maximum amount of \$1,000, the credit would reduce federal tax payable by \$140.

Non-refundable tax credits are valued at the lowest personal income tax rate because all taxpayers are subject to that rate for a portion of their taxable income. At a conceptual level, most non-refundable tax credits are designed to offset the tax that was paid on income in the first bracket used to pay for the expense. Applying a uniform credit rate ensures that taxpayers in similar circumstances receive the same amount of tax relief, independent of their income level or marginal tax rate. This differs from tax deductions, which reduce taxable income and therefore provide greater tax savings to individuals with higher marginal tax rates.

Impact of the Middle-Class Tax Cut on Non-Refundable Tax Credits

In 2026, the Middle-Class Tax Cut is estimated to provide nearly \$5.5 billion of tax relief to Canadians. The bulk of total tax relief will go to those with incomes in the two lowest tax brackets, including nearly half to those in the first bracket.²

For virtually all taxpayers, the tax savings from the lower tax rate exceed the decrease in the value of their non-refundable tax credits. As non-refundable tax credits are generally meant to offset tax on income used for eligible expenses, if less tax is owed on that income, then a smaller offset is required through the credits.

Example: An individual with \$60,000 of income in 2026 claiming only the Basic Personal Amount

The table below illustrates how reducing the lowest personal income tax rate from 15% to 14% affects an individual earning \$60,000 in 2026, assuming they claim only the Basic Personal Amount (BPA).

Table 3
Tax Calculation at 15% vs. 14%

	First Bracket Rate of 15%	First Bracket Rate of 14%
Step 1: Determining tax on income	First \$58,523 is taxed at 15%. Amount above that threshold is taxed at 20.5%.	First \$58,523 taxed at 14%. Amount above that threshold is taxed at 20.5%.
	Tax on income: \$9,081	Tax on income: \$8,496
Step 2: Claiming the BPA	BPA = \$16,452 Credit rate = 15% Credit value: \$2,468	BPA = \$16,452 Credit rate = 14% Credit value: \$2,303
Step 3: Determining tax owing	\$9,081 – \$2,468 = \$6,613	\$8,496 – \$2,303 = \$6,193
Overall impact		Tax Savings: \$420

As demonstrated in the example above, the maximum savings per year for an individual is \$420 and \$840 for a two-income family. How much any individual would save on average depends on certain factors, in particular their income level and their claims of non-refundable tax credits. For example, individuals with total taxable income in the first tax bracket would receive less than the maximum relief because their taxable income is less than the top of that bracket. Also, many individuals claim non-refundable tax credits in addition to the Basic Personal Amount, which reduces tax owed and thus potential tax savings from the rate reduction.

In the aggregate, the value of non-refundable tax credits falls by \$5.4 billion, which is more than offset by the reduction of income tax of \$10.6 billion.

² The analysis is based on the Department of Finance's T1 microsimulation model using 2023 individual tax filer data, and projects the impact of the middle-class tax cut on non-refundable tax credits for the 2026 taxation year (the first full year of the rate reduction).

Table 4

Cost of lowering the first tax rate and credit rate, 2026, for those paying tax

Taxable Income Group	Lowering first tax rate only (\$M)	Reduction in value of non refundable tax credits (\$M)	Middle-Class Tax Cut Impact (\$M)	Filers Paying Less Tax (M)
1 Up to \$58,523	3,615	-2,335	1,530	9.5
2 \$58,523 to \$117,045	5,165	-2,285	2,900	9.1
3 \$117,045 to \$181,440	1,210	-525	685	2.1
4 \$181,440 to \$258,482	360	-155	210	0.6
5 \$258,482 and over	295	-120	175	0.5
Total	10,645	-5,420	5,495	21.9

Notes. This does not include individuals subject to the Alternative Minimum Tax.

Total impact is not additive due to interactions among measures.

Table 5 below presents projected 2026 estimates of non-refundable tax credit claims and the associated change in tax relief resulting from a reduction in the credit rate from 15 per cent to 14 per cent. Non-refundable tax credits can only reduce tax payable and cannot generate a refund.

Table 5

Projected claims of non-refundable tax credits calculated at the lowest tax rate and associated relief, 2026 (\$000), for those paying tax

Name	Credit amount claimed (\$M)	Percentage of total credits claimed (%)	Change in credit value (\$M)
Basic Personal Amount	357,364	65.35	-3,542
Age amount	29,525	5.40	-293
Eligible dependant amount	10,213	1.87	-101
Spouse or common-law partner	15,495	2.83	-154
Caregiver amounts	1,930	0.35	-19
Base CPP or QPP contributions	43,143	7.89	-428
EI or QPIP premiums	13,680	2.50	-136
Volunteer firefighters' amount	249	0.05	-2
Search and rescue volunteers' amount	34	0.01	-0.3
Canada employment credit	24,636	4.51	-244
Home buyers' amount	1,555	0.28	-15
Home accessibility expenses	188	0.03	-2
Adoption expenses	9	0.002	-0.1
Pension income amount	9,735	1.78	-96
Disability amounts	8,681	1.59	-86
Student loan interest	172	0.03	-2
Tuition amounts and spousal transfers	13,368	2.44	-132
Medical expenses	16,886	3.09	-167
Total	546,863	100%	-5,420

Notes. Tax relief assumes that a 14-per-cent credit rate is applied to projected claimed amounts for 2026. Amounts claimed do not include those claimed by individuals expected to owe the Alternative Minimum Tax in 2026. The impact of reducing the value of each non-refundable tax credit is calculated by multiplying the total impact (\$5.42 billion) by each credit's share of the aggregate non-refundable credit amount.

Total projected claimed amounts of non-refundable tax credits in 2026 for those paying tax are estimated at \$546.9 billion. Applying a 14 per cent rate instead of 15 per cent is projected to reduce the total value of tax relief by approximately \$5.42 billion.

The Basic Personal Amount represents the most broadly claimed of non-refundable credits, with projected claimed amounts of \$357 billion, accounting for 65.4 per cent of total credits claimed. As a result, it also accounts for the largest share of the projected reduction in tax relief, at approximately \$3.5 billion. Other broad-based credits, such as those for base Canada Pension Plan or Quebec Pension Plan contributions, Employment Insurance or Quebec Parental Insurance Plan premiums, and the Canada Employment Credit, also contribute materially to the overall reduction due to their widespread use among working individuals.

Other credits, such as the volunteer firefighters' amount, home accessibility expenses, adoption expenses, and student loan interest, have relatively minor aggregate impacts due to their lower take-up.

The Top-Up Tax Credit

In very rare cases, where an individual has taxable income and non-refundable tax credit amounts that exceed the first income tax bracket threshold (\$58,523 in 2026), the decrease in the value of their non-refundable tax credits may exceed their tax savings from the middle-class tax cut. It is estimated that less than 0.3 per cent of tax filers would be in this situation.

This could happen in circumstances where an individual claims a large one-time expense, such as amounts for high tuition or medical expenses, or claims a combination of large tax credits. In some cases, these claims are both for themselves and a dependant, or include amounts carried forward from previous years. Taxpayers in these situations will benefit from the middle-class tax cut in future years.

To ensure that no one has their tax liability increased by the middle-class tax cut, and to help Canadians transition to the new lower rate, the government introduced a Top-Up Tax Credit for the 2025 to 2030 taxation years through Bill C-15, which received Royal Assent on March 26, 2026. The credit effectively maintains the current 15 per cent rate for non-refundable tax credits claimed on amounts in excess of the first income tax bracket threshold.

Conclusion

The reduction of the first marginal personal income tax rate, introduced in Bill C-4, also resulted in a lower non-refundable tax credit rate. Non-refundable tax credits are generally intended to offset tax on income used to pay for eligible expenses. Since the middle-class tax cut reduced the tax on income, the required offset is correspondingly lower.

For nearly all Canadians who pay tax, tax savings from the middle-class tax cut will outweigh the reduction in the value of non-refundable credits, resulting in maximum tax relief of \$420 per person, or \$840 per couple in 2026.

To ensure that no one is made worse off by the middle-class tax cut, the temporary Top-Up Tax Credit was announced in Budget 2025 and implemented through the passage of Bill C-15. In cases where individuals have non-refundable tax credit amounts and taxable income that exceed the first bracket threshold (\$58,523 in 2026), the Top-Up Tax Credit will effectively maintain the 15-per-cent rate for non-refundable tax credit amounts that exceed the first income tax bracket threshold.